

# ANALYSIS OF AMENDED BILL

Franchise Tax Board

Author: Cogdill Analyst: LuAnna Hass Bill Number: AB 1057  
Related Bills: See Legislative History Telephone: 845-7478 Amended Date: April 25, 2001  
Attorney: Patrick Kusiak Sponsor: \_\_\_\_\_

**SUBJECT:** Donations of Material, Equipment or Services for Highway Maintenance or Enhancement Credit

## SUMMARY

This bill would allow a credit for materials, equipment, or services that are donated by a taxpayer for roadside maintenance or enhancement.

## SUMMARY OF AMENDMENTS

The April 25, 2001, amendments would remove the language that would allow a deduction and replace it with language that would allow a credit for the same purpose.

This is the department's first analysis of this bill.

## PURPOSE OF THE BILL

The author's office has indicated that the purpose of this bill is to stimulate an increase in roadside beautification efforts from the private sector.

## EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective upon enactment and operative for taxable years beginning on or after its effective date.

## POSITION

Pending.

## ANALYSIS

### FEDERAL/STATE LAW

The Department of Transportation (DOT) oversees all highways that are under its jurisdiction, possession, or control. DOT may take any actions that are necessary, convenient, or proper for the construction, improvement, maintenance, or use of those highways.

Board Position:

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Department Director

Date

Gerald H. Goldberg

06/12/01

DOT may enter into agreements to accept funds, materials, equipment, or services from any person for maintenance or roadside enhancement of a section of a state highway. The agreement between DOT and any sponsor may specify the level of maintenance that will be performed and the director may authorize a courtesy highway sign for the sponsor. For a sponsor in Los Angeles or Orange counties, the director may authorize a demonstration program instead of the courtesy sign. The demonstration can either include the placement of sponsor recognition on the materials donated, other than safety equipment, or allow the sponsor to plant and maintain their individual organizational logo created from live plant materials.

Existing state and federal laws provide various tax credits designed to provide tax relief for taxpayers who incur certain expenses (e.g., child adoption) or to influence behavior, including business practices and decisions (e.g., research credits or economic development area hiring credits). These credits generally are designed to provide incentives for taxpayers to perform various actions or activities that they may not otherwise undertake.

Existing state and federal laws allow deductions from income for charitable contributions. Under certain circumstances an individual is allowed to deduct the fair market value of the property being contributed. An individual can deduct at most an amount equal to 50% of their adjusted gross income. The charitable contribution deduction for a corporation is limited to the adjusted basis of the property. In addition, the amount a corporation can deduct for a charitable contribution in a given year is limited to 10% of the corporation's net income. A contribution made by either an individual or a business in excess of the percentage limitations may be carried over and deducted in future years. No deduction is allowed for the value of services donated to a charitable organization.

### THIS BILL

This bill would allow a credit equal to 50% of the amount paid or incurred, or the fair market value of the materials, equipment, or services donated by a taxpayer for maintenance or roadside enhancement of a section of state highway.

### IMPLEMENTATION CONSIDERATIONS

This bill uses the term "fair market value" in relation to services donated. It is unclear what would constitute the fair market value of "time" if a person donates their personal time toward the maintenance or roadside enhancement of state highways.

Also, the department does not have any way to verify the amount of time spent on roadside maintenance. A method is needed to document the taxpayer's actual hours. The absence of a definition to clarify "fair market value" or verification of the hours could lead to disputes with taxpayers and would complicate the administration of this credit.

The type of materials and equipment used for roadside maintenance and beautification, such as gloves or gardening tools, are multi-purpose items. The department could not verify that these items are actually used for highway maintenance and thus eligible for the credit.

This bill would be operative for taxable years beginning on or after its effective date, which most likely would be a day in September or October of 2001. Tax credits are typically operative for taxable years beginning on or after January 1 of a particular year. It would be helpful if the bill were amended to contain the normal operative date language.

This bill would allow a credit equal to 50% of the amount paid or incurred, **or** the fair market value of the materials, equipment, or services donated. As a result, the bill could be interpreted to allow a 100% credit for the fair market value of the materials, equipment, or services donated. The author's staff has indicated that the intent of the bill is to allow taxpayer's to receive a credit of either 50% of the amount paid or incurred or 50% of the fair market value, whichever is greater. The author's staff has indicated the bill will be amended to reflect the intent of the author.

If this bill were amended to resolve these implementation considerations, implementing this bill would be accomplished during the normal annual update.

## OTHER STATES' INFORMATION

*Florida, Illinois, Massachusetts, Michigan, Minnesota, and New York* laws do not provide a credit or deduction comparable to the credit allowed by this bill. The laws of these states were reviewed because their tax laws are similar to California's tax laws.

## FISCAL IMPACT

If this bill were amended to resolve the implementation considerations addressed in this analysis, the bill would not significantly impact the department's costs.

## ECONOMIC IMPACT

### Tax Revenue Estimate

This proposal is estimated to impact Personal Income Tax revenue as shown in the following table.

Fiscal Year Cash Flow Impact Taxable Years Beginning After December 31, 2000 Enactment Assumed After June 30, 2001 \$ Millions			
Assumption	2001-02	2002-03	2003-04
\$5 Million In Donated Values	-\$2.5	-\$2.5	-\$2.5
\$10 Million In Donated Values	-\$5	-\$5	-\$5
\$15 Million In Donated Values	-\$7.5	-\$7.5	-\$7.5

This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this measure.

### Revenue Discussion

The revenue impact for this bill will be determined by the number of taxpayers who make donations, the value of those donations, and the tax liabilities of donors for applying tax credits.

Based on discussions with the Department of Transportation, there is no specific data regarding the value of donations made to highways, and it's unknown in advance how many taxpayers would donate materials, equipment, or their services to highways or roadside enhancement. Therefore, this estimate should be considered a rule of thumb.

First, three possible total fair market value donation amounts were assumed in the amounts of \$15, \$10 and \$5 million for each year. Second, the amount of credit is 50% of the amount paid or incurred or the fair market value. Third, it was assumed that contributors would be able to apply the full credit amount per year.

## **ARGUMENTS/POLICY CONCERNS**

This bill would provide a tax benefit for taxpayers that are subject to the Personal Income Tax Law, such as individuals, sole proprietorships, and noncorporate partners of partnerships. This same tax benefit would not be provided to other business entities that are subject to the Bank and Corporation Tax Law, such as corporations. Thus, this bill would provide differing treatment based solely on entity classification.

This bill would allow taxpayers a credit for the value of "time" as a service that is donated to the State for highway maintenance or enhancement, which is unprecedented. Credits generally are allowed to taxpayers for actual expenses paid or incurred. In addition, the credit taken by a taxpayer that donates services based on the number of hours donated could be construed as compensation from the State for those services. Unless specifically excluded, compensation for services is included in gross income and subject to tax.

Under existing law, a taxpayer contribution of property, including materials, equipment, or services may be limited to the cost paid or incurred by the taxpayer (basis) for the property. A credit that is based on the fair market value of the property contributed to the state as opposed to the basis could potentially be construed to be an amount realized on the disposition of that property, producing a gain subject to federal income tax.

By allowing the taxpayer to claim the proposed credit in addition to the charitable deduction allowed for the same expense, this bill would allow taxpayers to claim multiple tax benefits for the same item of expense in excess of the taxpayer's actual economic investment in the item.

This bill does not specify a repeal date. Credits typically are enacted with a repeal date to allow the Legislature to review their effectiveness.

This credit could not be carried over if the taxpayer does not use the entire credit amount in the year claimed. The author may wish to add language allowing a limited carryover period.

## **LEGISLATIVE STAFF CONTACT**

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